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BRETTON WOODS AGREEMENTS ACT AMENDMENTS AND INTERNATIONAL LENDING SUPERVISION

REPORT

OF THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

TO ACCOMPANY

S. 695

MAY 16, 1983.—Ordered to be printed

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Mr. GARN, from the Committee on Banking, Housing, and Urban Affairs, submitted the following

REPORT

[To accompany S. 695]

OVERVIEW OF THE INTERNATIONAL MONETARY FUND

General

The IMF was formed in 1944 to avoid a recurrence of the international trade and economic problems of the 1930's. Its purpose is to foster international monetary cooperation and to facilitate the expansion and balanced growth of international trade. The Fund is concerned with both the problems of individual member countries and the working of the international monetary system as a whole. In meeting these responsibilities, the IMF has both a regulatory and a financing function.

Regulatory function

In joining the Fund, countries agree to abide by a code of economic behavior, that includes cooperating with the Fund and each other to assure orderly exchange arrangements, and to avoid restrictions that would harm national and international prosperity. The Fund monitors this compliance, relying on the disbursal of its financial resources to exert leverage over countries to act in compliance with these principles. Membership in the Fund requires the furnishing of a broad range of economic and financial information on a continuing basis.

Financing function

Since a code of conduct alone cannot prevent payments imbalances and foreign exchange problems, the IMF maintains various financing facilities to help finance the temporary imbalances of members. None of these facilities are for development purposes. This financial assist-

ance—provided temporarily and usually subject to conditions—allows member countries to correct their payments imbalances/exchange rate problems without having to resort to the trade and payments distortions that they have pledged themselves to avoid. This assistance is then repaid to the IMF with interest (or a fee), and is thus available—as a revolving fund—for use by other members.

Structure

The IMF is an intergovernmental organization, based on an international convention called the Articles of Agreement. When a country joins the IMF it becomes a party to the Articles. Membership in the IMF is a prerequisite to membership in the World Bank. The work of the Fund is carried out through a Board of Governors, an Executive Board, a Managing Director, and a staff. Each member has a Governor and Alternate Governor on the Board of Governors, which meets annually. A member country's voting power is related to its subscription to the Fund's financial resources, which is based on a country's relative size in the world economy. The U.S. now has 19.52% of the voting power in the IMF, the only country with 15% or more, which is necessary for a veto on certain major decisions.

Quotas

Quota refers to a member's contribution to the general resources of the IMF, which in turn establishes the member's voting power in the IMF and ability to borrow from the IMF. Quotas are reviewed at intervals of not more than five years. General quota increases have occurred as follows:

	Percent
1959	50
1966	25
1970	25
1978	33
1980	50

Despite these periodic quota increases as a proportion of world imports, IMF quotas have fallen from 12 percent in 1960 to 3.8 percent in 1982. Quotas are paid to the IMF in the member's own currency, selected other currencies (e.g., dollars, sterling, German marks), and/or in Special Drawing Rights (SDR's, a reserve asset created by the IMF, whose value is determined by specific amounts of the five major international currencies—dollar, German mark, yen, pound sterling, and French franc). The Fund pays interest to a country for the use of its currency contribution.

Financing facilities

When a country draws on the IMF's financing facilities it purchases SDR's or other member's currencies from the IMF with the country's own currency (e.g., dollars purchased from the IMF by Mexico with Mexican pesos). The drawing member must repay the Fund by repurchasing other of its currency with SDR's or other specific currencies by the Fund (as specified by the IMF), plus a fee for the use of the currencies.

Tranches.—The first tranche, or reserve tranche, is what a member may draw from the IMF without any conditions, and it is equal to the portion of its quota that has not been subscribed in its own currency

or which has been used on a net basis by the Fund. The Fund's basic lending facility is a series of four additional credit tranches, each equal to 25 percent of a member's quota, that a country may draw on, by agreement from the Fund. Each successive credit tranche is subject to greater and more stringent conditions and supervision designed to aid a country eliminate the causes of its financial problems.

Extended facility.—A country suffering severe, structural problems, may, under agreement, borrow an additional 40 percent of its quota from the IMF, for a total of 140 percent credit drawing beyond the drawing of its reserve tranche.

Compensatory financing facility (CFF).—Offered to members whose export earnings have fallen for reasons beyond their control.

Enlarged access borrowing.—A temporary program, allowing a member with severe imbalance to draw up to 450 percent of its quota.

Buffer stock financing facility.—Available up to 50 percent of quota, assists members having payments difficulties to finance their contributions to international buffer stocks that are maintained to stabilize world markets for commodities, such as for tin and sugar.

General arrangements to borrow (GAB).—Ten industrial members (the G–10) stand ready to lend to the Fund to assist in meeting the balance of payments requirements of any one of them. At the recent meeting of the G–10 in Paris, on January 18, it also decided that the GAB would be revised to permit its use by the IMF to finance conditional drawings by any IMF member in the event there is an inadequacy of IMF resources to meet actual or expected requests for financing in exceptional circumstances to cope with or forestall an impairment of the international monetary system. The United States would have a virtual veto over the use of GAB resources in addition to its IMF veto power.

ECONOMIC BACKGROUND TO CURRENT DEBT CRISIS

During the last two decades the less developed countries (LDCs) have had a much faster growth rate than the economies of the industrialized countries. The average LDC growth rates in the 1960s and 1970s was 5½ percent in comparison to the 3 to 4 percent annual growth rates of the industrial economies. Some newly industrialized countries (sometimes called NICs), such as Brazil and Mexico, have had growth rates well above the LDC average as the result of the stimulation of massive foreign investment and aggressive development policies.

In the wake of the 1973 increase in oil prices, the non-OPEC LDCs tried to expand their industrial base rapidly to cope with the needs of their growing populations and to increase their national income which had been adversely affected by increased energy costs. This led to a surge in commercial bank lending to the LDCs, as the higher oil prices and ensuing world recession quadrupled the current account deficit from about $11 billion in 1973 to over $45 billion in 1975. Bank lending to LDCs prior to the 1970s was largely confined to short term trade financing, a few long term loans to governments extended mainly in conjunction with IMF stabilization programs, and a modest amount of project-related loans, frequently guaranteed by third-parties.

Previously this short-term, balance of payments financing had been handled by institutions such as the International Monetary Fund, but the official funds available were inadequate and Western governments were concerned that the OPEC current account surplus, which jumped from $7 billion in 1973 to $68 billion in 1974, would continue indefinitely. This, in turn, threatened to undermine the international financial system in the absence of some mechanism to "recycle" these "petrodollars." In these years, apprehensions concerning commercial banks centered on the liability rather than the asset side of the ledger, with fears expressed about the volatile, short-term nature of the deposits rather than the shakiness of the LDC economies and their public and private economic projects.

In fact, while LDC debt to foreign banks rose rapidly in the post-1973 period (from about $35 billion in 1973 to $270 billion in mid-1982), these countries were also able to add $40 billion to their reserves during those years, which tended to maintain confidence in their financial management and outlook.

However, the second great oil price increase at the end of the 1970s called into question some of the favorable assumptions of both borrowers and lenders.

In 1980 the industrialized nations entered into a recession from which they are now just emerging. World trade declined in volume for only the second time in the postwar era. This had a direct effect on the LDC economies, which rely heavily on commodities for income. Commodity prices fell 30 percent to their lowest levels in a generation.

The increased oil prices led to further LDC current account deficits. However, the industrial nations, and particularly the United States, proved unwilling to respond to the second oil shock with accommodative policies to the extent that they had so responded to the first oil shock. Economic policy-makers in the major industrial states became convinced that the upward ratcheting of inflation had to be brought to an end. But, because of the intractability of government spending, the burden of fighting inflation was borne almost entirely by restrictive monetary policies, which exacerbated the effects of the worldwide inflation which began in the late 1970s. This, in turn, culminated in record-high nominal and real interest rates. Real short-term rates increased from approximately .5 percent in 1977 to the 5 percent range in 1981, and real long-term rates went from about 1.5 percent to 5 percent during the same period.

IMPLICATIONS FOR U.S. BANKS

As a result of the great confidence in LDC credit-worthiness felt by the commercial banks that developed in the late 1970s, bank lending to LDC expanded rapidly, at a nearly 20 percent rate of increase. The vast majority of this lending was concentrated among certain borrowers judged to be the most credit-worthy—Mexico, Brazil, and Argentina. The nine largest U.S. banks' claims on these three countries rose at average annual rates of 35, 15, and 30 percent respectively, between year-end 1979 and mid-1982.

Compounding this concentration was the fact that most of the increase over this period was in the form of short-term credits. While they seemed less risky than medium and long-term credits and while

they were attractive to the LDCs in times of high interest rates, they also increased the borrowers' vulnerability to a sudden reduction in the willingness of lenders to roll over existing debt. Moreover, short-term lending provided little protection for the banks as a group, since they could not all attempt to withdraw such credit at the same time without provoking a liquidity crisis for the borrowers.

Throughout this period, losses of foreign loans of commercial banks continued to be substantially lower than on domestic lending. Foreign lending accounted for a rising share of the assets and the earnings of most large U.S. banks. But the loans were highly concentrated. Of the $270 billion owed to banks by public and private sector borrowers in all developing countries at mid-1982, over half was accounted for by three countries: Mexico, Brazil, and Argentina. Eastern Europe owed another $64 billion to Western banks, but the U.S. bank share amounted to only slightly more than 10 percent.

NEED FOR INCREASE IN U.S. PARTICIPATION IN IMF

The most coherent and convincing case for the proposed increase in U.S. participation in the IMF was put forward by Secretary of the Treasury Donald Regan in his testimony of February 14, 1983. In defending the Administration's proposal to increase the U.S. quota for the IMF from the current 12.6 billion SDR to 17.9 billion SDR and participation in the IMF's General Arrangements to Borrow (GAB) from the current 1.55 billion SDR to 4.25 billion SDR, a combined increase totalling nearly $8.5 billion at current exchange rates, Secretary Regan outlined the problems facing the international financial system and the key role the IMF must play in resolving the problems. Secretary Regan made the point that the IMF was created in 1944 with great impetus from the United States in order to offer a backstop and support mechanism to prevent a recurrence of the depression of the 1930s, and, "if the IMF is to be able to continue in that role it must have adequate resources to deal with the current international financial situation."

Explaining the importance to the U.S. of an orderly resolution to the international financial problem, Secretary Regan outlined the problem. "First, a further abrupt and largescale contraction of LDC imports would do major damage to the U.S. economy. Second, if the situation were handled badly, the difficulties facing LDC borrowers might come to appear so hopeless that they would be tempted to take desperate steps to try to escape. The present situation is manageable. But a downward spiral of world trade and billions of dollars in simultaneous loan losses would pose a fundamental threat to the international economic system, and to the American economy as well."

Total U.S. bank claims on the LDCs in June 1982 were about $100 billion, of which the nine largest banks accounted for 60 percent and the next 15 banks an additional 20 percent. As the Federal Reserve Board has noted, claims on the LDCs for the nine largest U.S. banks amounted to 200 percent of their capital by mid-1982, with about half of those claims on Mexico, Argentina, and Brazil.

IMPLICATIONS OF LDC DEBT FOR U.S. TRADE

The current debt crisis is certain to have an adverse effect at least in the short run on U.S. export earnings. This could have a very signifi-

cant impact on U.S. economic recovery. It should be remembered that the share of trade in our GNP more than doubled during the 1970s, from less than 4 percent to more than 8 percent. Over half of the total growth in the U.S. economy from 1978–80 came from the improvement in exports, while the recession of 1981–82 has been led by a deterioration in that sector, a larger factor in the recession than the housing or auto sector slumps.

Obviously, the debt crisis has had a severe effect on U.S. exports to the LDC market. For example, exports to Mexico, the third largest U.S. export market, were down 26 percent in the first eight months of 1982. U.S. sales to Argentina were off 50 percent. Only Brazil has continued to be a relatively robust U.S. export market with sales down only 10 percent for the same period.

Commenting on the importance of LDCs having access to IMF capital markets to finance short-term balance-of-payments shortfalls to fund imports Secretary Regan noted:

> Among the most important export sectors for this country are agriculture, services, high technology, crude materials and fuels. American agriculture is heavily export-oriented: one in three acres of U.S. agricultural land, and 40 percent of agricultural production, go to exports. This is one sector in which we run a consistent trade surplus, a surplus that grew from $1.6 billion in 1970 to over $24 billion in 1980.
>
> Vigorous expansion of our export sectors has become critical to employment in the United States. The absolute importance of exports is large enough—they accounted directly for 5 million jobs in 1982, including one out of every eight jobs in manufacturing industry. But export-related jobs have been getting even more important at the margin. A survey in the last 1970s indicated that four out of every five new jobs in U.S. manufacturing was coming from foreign trade; on average, it is estimated that every $1 billion increase in our exports results in 24,000 new jobs.
>
> These figures serve to illustrate the overall importance of exports to the U.S. economy. The story can be taken one step further, to relate it more closely to the present financial situation. Our trading relations with the LDCs have expanded even more rapidly than overall trade. Our exports to the LDCs, which accounted for about 25 percent of total U.S. exports in 1970, rose to about 29 percent by 1980. In manufactured goods, which make up two-thirds of our exports, the share going to LDCs rose even more strongly—from 29 percent to 39 percent. In fact, since the mid-1970s trade with LDCs has accounted for more than half of the overall growth of American exports.
>
> What these figures mean is that the export sector of our economy—a leader in creating new jobs—is tremendously vulnerable to any sharp cutbacks in imports by the LDCs. Yet that is exactly the response to which debt and liquidity problems have been driving them. This is a matter of concern not just to the banking system, but to American workers, farmers, manufacturers and investors as well.

Secretary Regan defined the Administration's strategy to resolve the existing international financial problem. Key to the strategy is an increase in the IMF quota. Regan said:

> We have been working on a broad-based strategy involving all the key players—LDC governments, governments in the industrialized countries, commercial banks, and the International Monetary Fund. This strategy has five main parts:
>
> First, and in the long run most important, must be effective adjustment in borrowing countries. In other words, they must take steps to get their economies back on a stable course, and to make sure that imports do not grow faster than their ability to pay for them . . . orderly and effective adjustment will not come overnight. The adjustment will have to come more slowly, and must involve expansion of productive investment and exports.
>
> The second element in our overall strategy is the continued availability of official balance of payments financing, on a scale sufficient to help see troubled borrowers through the adjustment period. The key institution for this purpose is the International Monetary Fund. The IMF not only provides temporary balance of payments financing, but also assures that use of its funds is tied tightly to implementation of needed policy measures by borrowers. It is this aspect—IMF conditionality—that makes the role of the IMF in resolving the current debt situation and the adequacy of its resources so important.

Amplifying on the role of the IMF, Secretary Regan pointed to a very important function:

> * * * [t]he conditionality attached to IMF lending is designed to assure that orderly adjustment takes place—and that the borrower is restored to a position which will enable it to repay the IMF over the medium-term. In addition, a borrower's agreement with the IMF on an economic program is usually viewed by financial market participants as an international "seal of approval" of the borrowers policies, and serves as a catalyst for additional private and official financing.
>
> Thus, the third element in our strategy is the willingness of governments and central banks in the lending countries to act quickly to respond to debt emergencies when they occur. Recent experience has demonstrated the need to consider providing immediate and substantial short-term financing—on a selective basis, where system-wide dangers are present—to tide countries through their negotiations with the IMF and discussions with other creditors. We are undertaking this where necessary, on a case-by-case basis, through ad hoc arrangements among finance ministeries and central banks, often in cooperation with the Bank for International Settlements. But it must be emphasized that these lending packages are short-term in nature, designed to last for only a year at most and normally less, and cannot substitute for IMF re-

sources which are designed to help countries through a multi-year adjustment process.

In fact, IMF resources themselves have only a transitional and supporting role. The overall amount of Fund resources, while substantial, is limited and not in any event adequate to finance the needs of its members. While we feel that a sizable increase in IMF resources is essential, this increase is not a substitute for lending by commercial banks. Private banks have been the largest single source of international financing in the past to both industrial and developing countries, and this will have to be the case in the future as well—including during the crucial period of adjustment.

Thus, the fourth essential element in resolving debt problems is continued commercial bank lending to countries that are pursuing sound adjustment programs. In the last months of 1982 some banks, both in United States and abroad, sought to limit or reduce outstanding loans to troubled borrowers. But an orderly resolution of the present situation requires not only a willingness by banks to "roll over" or restructure existing debts, but also to increase their net lending to developing countries, including the most troubled borrowers, to support effective, non-disruptive adjustment. * * * Without this continued lending in support of orderly and constructive economic adjustment, the programs that have been formulated with the IMF cannot succeed—and the lenders should be noted, however, that new bank lending will be at a slower rate than that which has characterized the last few years—more in line with the increase in 1982 than what we saw in 1980 or 1981.

The final part of our strategy is to restore sustainable economic growth and to preserve and strengthen the free trading system. The world economy is poised for a sustained recovery: inflation rates in most major countries have receded; nominal interest rates have fallen sharply; inventory rundowns are largely complete.

Finally, Secretary Regan argued:

The IMF is essentially a non-political institution, with membership open to any country judged willing and able to meet the obligations of membership. But this does not mean that U.S. political and security interests are not served by the IMF. On the contrary—it serves our interests well by containing economic problems which could otherwise spread through the international community; minimizing political instability in countries facing the inevitable social and economic dislocations which accompany adjustment; and supporting open, market-oriented economic systems consistent with Western political values. Judged on this criterion, U.S. appropriations for the IMF can be an excellent investment if they can help to avoid political upheaval in countries of critical interest to the United States.

COMMITTEE COMMENTS

The Committee has approved a substantial increase in the United States' contribution to the International Monetary Fund with the understanding that the current round of increases—although necessitated, in part, by short-term requirements—are required to help achieve long-term stability in the international financial marketplace. The Committee wishes to emphasize that its approval of the increase is predicated on the expectation that the operations of the Fund will be directed toward achieving this long-term goal and avoiding the need for another request for increased contributions in the near term. While the Committee recognizes the need for periodic adjustments in IMF quotas in line with the growth in world trade and payments, it wishes to reduce the possibility of repeated calls for additional financing, and accordingly directs the Secretary of the Treasury and the Chairman of the Federal Reserve Board to report to the Committee at timely intervals on progress being made toward the long-term goal of achieving a better balance in the pattern of international payments through a reduction in the size of payments imbalances.

The economic growth of Third World countries depends on financial support from the industrialized nations. The Third World countries, in turn, provide expanded markets for the industrialized nations' products.

This economic interdependence is jeopardized when investment practices of lending institutions in the industrialized nations foster the use of their financial resources to support fundamentally uneconomic Third World development projects. The further consequences of such investment practices are to deprive these Third World countries of some of their best growth potential, to severely penalize economic industries in the industrialized nations and to endanger repayment of many of the investments.

Many of these foreign financing problems have arisen because some lending institutions, including some U.S. banks, failed to apply consistently reasonable standards which took into consideration project economics and the impact of such projects on the economies of the borrowing and lending nations, and thereby also failed to assess the intrinsic viability of such projects and to eliminate financings of any foreign project which were made to appear viable only through subsidies from the host foreign country.

The Committee notes that such practices are detrimental not only to the developing nations themselves but also to the economic health and viability of key industries in the United States, such as the copper and steel industries. In the past such industries have been adversely affected by world overproduction of their products. It is the Committee's expectation that the enhanced examination procedures mandated by this bill will force banks to better assess the economic viability of projects they finance, which, in turn, will lead to a positive effect on U.S. economic health as fewer projects with questionable economic viability are financed.

The Committee notes with concern the recent trends toward export subsidization and protection among developing nations. To help com-

bat these adverse practices the Committee added two amendments to the Bretton Woods Agreements Act. The first amendment calls on the Secretary of the Treasury to instruct the United States Executive Director to the Fund to present proposals aimed at ensuring that member countries take steps to eliminate all import restrictions which have a serious adverse impact on U.S. exports or employment. The amendment also calls for a study of import restrictions and subsidies with such serious adverse impact on U.S. exports or employment by the U.S. Trade Representative, the Secretary of Labor, and the Secretary of Commerce in order to facilitate these instructions.

The Committee also approved a second amendment which calls on the Secretary of the Treasury to instruct the U.S. Executive Director to the Fund to initiate consultation with the Managing Director and other directors of the Fund with the goal of developing financial and technical assistance policies which will reduce obstacles and restrictions on international trade and investment, eliminate unfair trade and investment practices, and promote mutually advantageous economic relations. It is the Committee's expectation that these two amendments will help the effort which has gone on since World War II to create a freer trading and investment environment in the world, not only for the benefit of the United States but for the benefit of the entire community of trading nations.

COMMITTEE ACTION

The Committee began its consideration of the anticipated IMF quota increase with two briefings by Under Secretary of the Treasury for Monetary Affairs Beryl W. Springel, on January 3, and on January 25, 1983. Dr. Sprinkel briefed the Committee on the role of the IMF and the probable need for the U.S. to participate in an increase in the Fund's resources.

The formal hearing process began on February 14, 1983. Secretary of the Treasury, Donald Regan presented testimony to the Subcommittee on International Finance and Monetary Policy on the Administration's proposal for legislation to increase the resources of the IMF. He addressed the international financial situation and the steps that were being taken to strengthen it. The hearings continued on February 15, 1983, with testimony given by Lionel Olmer, Under Secretary for International Trade of the Department of Commerce. Also, at this same hearing, testimony was given by Mr. George Champion, former Chief Executive Officer of the Chase Manhattan Bank; Martin P. Mayer, Consultant and author; Richard A. Debs, President of Morgan Stanley International; William J. McDonough, Executive Vice President, First National Bank of Chicago; and George J. Clark, Executive Vice President of Citibank. Two days later, on February 17, 1983, the Subcommittee heard from the banking system regulators, Paul A. Volcker, Chairman of the Federal Reserve System; C. T. Conover, Comptroller of the Currency; and William Isaac, Chairman of the Federal Deposit Insurance Corporation, who discussed not only the current international financial situation but also the bank regulatory issues associated with that situation.

The banking regulators returned to testify before the full Committee on April 11, at which time they discussed specific regulatory changes they proposed in a joint memorandum. Subsequently, at the request of the Committee, the regulators resubmitted the memorandum in the form of draft legislation, which became the core of the Committee Print used at the mark-up on April 28.

During the April 28 mark-up session, Senator Hawkins proposed four amendments:

(1) A proposal to increase the IMF/GAB by only $4.2 billion (rather than $8.4 bilion); (2) a proposal to urge the creation of an IMF gold lending facility; (3) a proposal to return one-third of the Fund's gold to the contributing nations; and (4) a proposal for the Secretary of Treasury and the Federal Reserve Chairman to conduct a study for the Congress on the impact rising gold prices have on the reserves of gold held by the world's central banks.

Senator Hawkins subsequently withdrew the amendments, reserving her right to offer them on the floor.

Senator Mattingly offered two amendments during the mark-up session, both of which were agreed to. The first of his amendments will have the Secretary of the Treasury instruct the U.S. Executive Director to the Fund to initiate action to reduce obstacles to and restrictions upon international trade and investment. Senator Mattingly's other amendment requires the Secretary of the Treasury to transmit an annual report to the Congress on the success in reducing or eliminating the obstacles, restrictions and unfair trade practices.

Senator Proxmire, on behalf of Senators Sarbanes and Dodd offered an amendment on the establishment within the IMF of a schedule of customary fees and interest charges. The amendment would provide member countries with assistance in determining what were reasonable and customary rates of interest and front end fees to pay in the course of restructuring loan arrangements. Senator Proxmire withdrew the proposed amendment but preserved the right of the Senators to offer it on the floor when the legislation is considered.

The Committee voted to report the bill as amended by a vote of 15–0, with Senators Armstrong, Hawkins and Mattingly voting "present."

INTERNATIONAL LENDING SUPERVISION

As outlined above, in hearings on the source of the problems that some countries recently have experienced in servicing their external debts, the Committee found that the problems originated in the worldwide inflationary pressures that were allowed to develop after the oil price shocks of 1973–74 and especially of 1979–80.

Sharply higher oil import costs meant that importing nations would have to use a larger percentage of their domestic economic resources to pay for oil imports. To postpone the declines in domestic standards of living and/or declines in domestic capital formation which would result, some countries borrowed abroad. This was encouraged by the expectation that repayments could be made in the future with dollars and other foreign currencies whose real values had been eroded by inflation.

Rising balance of payments deficits of oil importing nations were matched by the surpluses of the oil exporters. The latter chose to invest their surpluses in the industrialized countries, to a significant extent, in

commercial bank deposits. These deposits were the primary source of the funds loaned to the developing countries that were stepping up their foreign borrowings to finance oil imports.

The expectation that foreign borrowings could be repaid with depreciated currencies also prompted some countries to increase their borrowings abroad in order to finance capital imports and, thereby, to accelerate their domestic economic growth rates.

A lack of timely data on the total external indebtedness of individual countries contributed to commercial banks' problems in keeping fully abreast of the gross foreign borrowings of some countries and hampered those banks' ability to exercise sufficient restraint on borrowing countries.

Worldwide inflation eventually and foreseeably led to escalating interest rates and worldwide recession. These two developments seriously affected the debtor countries. Their ability to earn foreign currencies by exporting was cut sharply at the same time that the rising cost of debt service greatly increased their need for those foreign currencies. Less developed countries that tend to be particularly dependent on commodity exports were particularly hard-hit by the recession and the attendant drop in commodity prices.

The central banks of some of these countries found that their net exports simply were not generating a sufficient quantity of foreign currencies to meet the requirements of public and private sector borrowers to make interest and principal payments on their foreign debts. This is a risk that is unique to international lending: known as "transfer risk"; it is the risk that a borrower, even if he has no shortage of his own domestic currency, will not be able to purchase the foreign currency needed to service his debt to a foreign creditor.

The gross external debt of less developed countries now totals approximately $550 billion. It includes obligations ranging from short-term credit to loans that do not mature for 10 to 20 years. It includes obligations owed to governments and official institutions like the IMF and the World Bank, as well as those due to commercial banks from various countries. The portion of debt owed to governments and official institutions is estimated at more than 35 percent of the total—or some $200 billion. Of the remaining $350 billion, $270 billion is owed to banks. Approximately one-third of that bank debt is due to U.S. banks.

C. T. Conover, Comptroller of the Currency, noted in his testimony before the Committee that:

> In 1979, the three banking agencies established the Interagency Country Exposure Review Committee (ICERC) to evaluate transfer risk and incorporate that evaluation into bank supervision.

Paul A. Volcker, Chairman of the Board of Governors of the Federal Reserve System told the Committee, however, that:

> * * * the rapid development of international lending and today's problems do point to the need for careful review of present policies and other ideas.

In a subsequent "Joint Memorandum" to the Committee, the three Federal bank regulatory agencies outlined a five-point program that they had developed to improve supervision and regulation of international leading.

The Committee concluded that the recent debt-service problems being experienced by some countries indeed does provide clear evidence that improvements are needed in the supervision and regulation of international lending.

Moreover, while the Committee concurred with the five-point program outlined by the regulators, the Committee also concluded that specific legislative action is needed to mandate permanent improvements in the supervision and regulation of international lending, to improve the timeliness and comprehensiveness of public information on foreign borrowing and lending, and to assure that appropriate accounting procedures are used to report the true results of international lending.

With regard to public information, the Committee found that better information is needed by the banks on total external indebtedness of individual countries and by the marketplace on an individual bank's exposure in a country once a threshold percentage of the bank's assets is passed.[1]

At the same time, however, the Committee concluded that great care should be taken not to complicate upcoming debt restructurings or to impede future prudent growth in foreign lending that is essential to the growth of U.S. exports and export-related jobs, and to the growth of the U.S. and the world economy.

STRENGTHENED SUPERVISION OF INTERNATIONAL LENDING

In light of the transfer risk associated with foreign lending which has been highlighted by the recent liquidity problems of some countries, the legislation specifically directs each of the federal banking agencies to incorporate "country exposure and transfer risk" in its examination and supervision procedures. The Committee expects that an effective system of country exposure warnings will be adopted as part of the examination process that assures these warnings are considered at the policy-making level. This system of country exposure warning should recognize that certain country exposure may be subject to greater levels of transfer risk than others, depending on domestic economic policies and conditions, as well as other factors, in a particular country. The legislation also directs the banking agencies to include considerations of country exposure and transfer risk in evaluations of capital adequacy, while recognizing that such factors as diversification of foreign credits clearly are important in assessing the amount of capital needed by an individual bank.

RESERVES

Commercial banks currently establish reserves as a precaution against possible losses, and the worldwide economic problems described above have led banks to increase these reserves substantially in recent years. The 25 largest American banks alone, for example, increased their reserves for losses on both domestic and international credits by $925 mililon in 1982. Still, in light of the extremely high

[1] In their reporting requirements on country exposure, the federal banking agencies currently define such exposure in a country as all cross-border and cross-currency claims and contingent claims on residents of a country, plus other credits guaranteed by residents of the country, less credits guaranteed by residents of other countries and net local currency assets of the banking institution's offices in the country.

transfer risk now associated with loans to certain countries, the Committee concluded that a new "special reserve" was needed for these credits.

The bill provides that each appropriate federal banking agency shall require a banking institution to establish and maintain a special reserve whenever, in the judgment of the agency, the institution's exposure in a particular country has become subject to a level of transfer risk that indicates a protracted inability of borrowers to make scheduled payments on external indebtedness.

These special reserves are to be established by a provision against current income, and they are not to be considered as part of capital or allowances for loan losses for regulatory, supervisory or disclosure purposes.

Protracted inability to make payments would be indicated by such factors as: (a) a failure of borrowers to make full interest payments on indebtedness for a substantial time period such as six months or more, (b) the terms of restructured indebtedness have not been met for over one year, (c) an IMF or other suitable adjustment program has not been complied with and there is no immediate prospect for such compliance, or (d) no definite prospects exist for the orderly restoration of debt service in the near future.

As an alternative to establishing special reserves, a bank would have the option to write off all or part of the loans that would be subject to special reserves and, thereby, reduce the amount of special provisions and reserve balances that otherwise would be required. These special reserves would not apply, for example, to lending to a country where the terms of any restructuring of debt are being met, where interest payments are being made regularly, and where the borrowing country is complying with the terms of an IMF-approved stabilization program.

Reschedulings are not uncommon on either domestic or international loans, for while future cash flows can be forecasted to some extent, the forecasted cash flows sometimes are not achieved in the out-years of a loan repayment schedule. When this occurs, the loan may need to be refinanced, restructured, or rescheduled. A number of domestic loans have had to be rescheduled as a result of the same volatility in interest rates and commodity prices and the same recession in economic activity that has forced the rescheduling of foreign credits. This does not necessarily mean that either the domestic loans or the foreign loans are bad debts.

Imposing special reserves on international loans whenever there is a rescheduling would be inconsistent with current treatment of domestic loans. Much more serious, such a reserve requirement would hamper the ability of banks to work with financially troubled borrowers, increase the costs of reschedulings to those financially troubled borrowers, and weaken the prospects for successful reschedulings.

ACCOUNTING FOR FEES ON INTERNATIONAL LOANS

The bill provides that each appropriate federal banking agency shall establish rules or regulations for accounting for fees charged by banks in connection with international loans. In general, under these rules or regulations, any portion of a fee that is deemed to represent interest income should be amortized over the effective life of

the loan, recognizing that the effective life may differ from the loan's stated term. Under these rules and regulations, income received for the performance of services during one accounting period should not be deferred until subsequent accounting periods. In seeking to achieve these objectives, the banking agencies have been given authority to define accounting rules; the bill does not attempt to do so by statute.

It is the Committee's understanding that the Financial Accounting Standards Board may soon consider proposed changes in accounting treatment of nonreimbursable loan fees, such as front-end fees on international credits. Accordingly, the Committee expects the federal banking agencies to adopt accounting rules that take into account the most current thinking of the accounting profession, and to adapt such rules as necessary to changing industry practices.

SECURITIES LAWS

The Committee has considered the possible impact of the legislation, specifically reserves and fees, on the federal securities laws and generally accepted accounting principles (GAAP), and has determined that nothing in this legislation should be construed as setting disclosure requirements under the federal securities laws or accounting principles for GAAP.

COLLECTION AND DISCLOSURE OF CERTAIN INTERNATIONAL LENDING DATA

In order to enhance the bank supervisory agencies' capacity to analyze and assess developing trends in international lending and to supervise better the banking institutions involved, the bill authorizes the agencies to require more frequent reports from banking institutions with respect to foreign country exposure. Currently, country lending reports are required on a semi-annual basis, whereas this legislation would require such reports to be filed no fewer than four times a year.

The bill also directs the bank supervisory agencies to require public disclosure of information regarding material country risk exposure in relation to the assets and capital of the banking institution. The Committee notes that such disclosure requirements are separate from those required under SEC authority but, of course, similar information may be required by the SEC. Public disclosure will enhance marketplace discipline by providing depositors and investors with information upon which to assess the banking institutions' foreign lending. Banks will need to be prepared to defend policies leading to large and concentrated country exposure. Recognizing the relationship of disclosure to the financial and competitive condition of the bank, however, the bill grants to the three banking agencies the authority to determine the form and type of information which must be disclosed.

INTERNATIONAL COOPERATION

Current problems in foreign lending are international in scope, and an effective program for dealing with those problems in the future must be coordinated with bank supervisors abroad and with the activities and operations of the International Monetary Fund. The bill

accordingly calls upon the Secretary of the Treasury to instruct the U.S. Executive Director of the Fund to propose the adoption of a number of policies that can give the Fund a greater role in helping to avoid situations involving excessive build-ups of credit, especially short-term. The bill also calls on the Federal banking agencies to consult with foreign bank supervisory authorities to coordinate supervisory policies and practices with respect to international lending.

CAPITAL ADEQUACY

In addition to the provisions dealing specifically with international lending, the legislation also requires the bank regulatory agencies to establish uniform systems for requiring banks to maintain adequate levels of capital. The Committee believes this positive mandate is necessary to insure that banking institutions, and especially larger banks, are adequately capitalized.

Figures published by the Federal Reserve indicate that capital ratios declined at larger banks throughout most of the 1970's as bank capital failed to grow as quickly as inflation-spurred growth in bank assets. These ratios, however, increased somewhat in 1981 and 1982, due largely to a significant slowdown in asset growth. Unpublished Federal Reserve data show an acceleration in the growth rate of capital ratios for the largest banks since mid-1982.

The Committee also believes clarification of existing authority is needed because the recent decision of the U.S. Court of Appeals (Fifth Circuit) in First National Bank of Bellaire v. Comptroller of the Currency has clouded the authority of the bank regulatory agencies to exercise their independent discretion in establishing and requiring the maintenance of appropriate levels of capital.

In Bellaire, the Court set aside the Comptroller's judgment as to what constitutes a safe and sound level of capital. The Committee believes that establishing adequate levels of capital is properly left to the expertise and discretion of the agencies. Therefore, in order to clarify the authority of the banking agencies to establish adequate levels of capital requirements, to require the maintenance of those levels, and to prevent the courts from disturbing such capital, the Committee has provided a specific grant of authority to the banking agencies to establish levels of capital for categories of institutions or individual institutions. In carrying out this authority, the banking agencies are expected to give banks reasonable time periods to meet any requirements for higher capital ratios.

In carrying out the authority under this Act, the Committee does not expect the bank regulatory agencies to adopt a single, uniform capital ratio that will apply to all banks regardless of their individual characteristics. Capital adequacy standards must necessarily take into account difference in risk diversification, asset quality, liability composition, and other factors considered relevant to capital adequacy. Nevertheless, the Committee expects the standards developed under this Act will be uniform among the three bank regulatory agencies, so that banks with the same characteristics are treated alike regardless of their regulatory status.

GENERAL AUTHORITIES

The bill provides rulemaking authority to the federal banking agencies for purposes of carrying out their authorities under this Act and, in addition to such other existing authority as each agency may have, the bill expressly provides for the availability of the authorities contained in Section 8 of the Federal Deposit Insurance Act for each agency to ensure compliance with the new statute and any rules, regulations or orders issued thereunder.

The provisions of the bill are, by their terms, applicable to all insured banks (as that term is defined in Section 3(h) of the Federal Deposit Insurance Act), any subsidiary of an insured bank, and any Edge or agreement corporation. In addition, to the extent determined by the federal banking agencies, any provisions of the bill may be applied as appropriate to any agency or branch of a foreign bank or any commercial lending company owned or controlled by one or more foreign banks or companies that control foreign banks, but not a foreign bank. In addition, in order to promote uniform application of the statute or prevent evasions thereof, any of the provisions of the bill may be applied by the appropriate federal banking agency to any affiliate of any insured bank, including any bank holding company individually or on a consolidated basis or its non-bank subsidaries, for which affiliate it is the appropriate federal banking agency. However, "affiliate" is not intended to include foreign affiliates that are not owned or controlled directly or indirectly by a U.S. banking organization.

The supervisory responsibilities of the appropriate federal banking agencies for their respective banking institutions are confirmed in the bill, and nothing in the legislation is intended to derogate from existing statutory authorities. Against this background, the bill requires the agencies to establish appropriate uniform principles and objectives for implementation of their respective authorities under this law, recognizing the need for agencies to have flexibility to deal with special circumstances that might arise. The agencies are, for three years, to report annually to this Committee and to the Committee on Banking, Finance, and Urban Affairs of the House of Representatives on actions taken to implement this legislation, including any actions that are inconsistent with its uniform implementation. This forum should be adequate for resolving any significant differences among the agencies. The Committee expects, however, that the three agencies will exert their best efforts to achieve uniform implementation of the authorities contained in this Act. The agencies may also recommend further legislative action as necessary to address the concerns reflected in this bill.

SECTION-BY-SECTION ANALYSIS

The following is a section-by-section description of major provisions of the bill.

Title I, Section 101(a) amends Section 17 of the Bretton Woods Agreements Act by authorizing an increase in U.S. participation in the General Arrangements to Borrow as amended. (a) (2) and (3)

authorize the Treasury to make resources available to the IMF to finance transactions in an amount not to exceed the equivalent of SDR 4.25 billion ($4.7 billion) as are appropriated in advance in appropriations acts. (a)(4) adds a new subsection at the end of Section 17, subsection (d) which will require the Secretary of the Treasury to seek advance Congressional authorization prior to consenting formally to any amendment to the GAB arrangement where that amendment significantly alters the amounts, terms, or conditions of U.S. participation in the GAB. This section is not meant to require prior approval for minor technical amendments to the arrangement, such as alterations of interest charges or payments which simply reflect changed market conditions, nor is it meant to require prior approval for additional lenders to join the arrangement or participate in some parallel manner.

Section 101(b) as amended by the Foreign Relations Committee adds three new sections to the end of the existing Bretton Woods Agreements Act.

The first new section, Section 40, authorizes an increase in the quota of the U.S. in the IMF in the amount of SDR 5.3108 billion (approximately $5.8 billion). It authorizes appropriations for the dollar equivalent of the SDR increase in the quota, and is worded such that the Appropriations Act will provide the full SDR amount as budget authority.

The second new section, Section 41, (a) provides instructions to the U.S. Executive Director to discuss, propose, and vote for the adoption of procedures within the Fund which will improve the quantity and quality of financial information available to the Fund concerning cross-border lending and borrowing.

The provisions of Section 41(b), in particular, are intended to strengthen reporting on cross-border foreign exchange credits, i.e., borrowing or lending in currencies other than the currency of the country in which the borrower is principally established or local currency borrowing by a business not principally located in the country but which borrowing is made in support of such business, in order to permit more accurate assessment of countries' external debt positions. It is assumed that appropriate exclusions would be made for minor transactions and/or transactions by certain classes of borrowers, such as private individuals, whose transactions would not be expected to have a significant impact on the overall external debt position of borrowing countries.

Section 41(c) defines credit as any outstanding loan, either short term or long, to the private or public sectors of a member. It also includes any unused lines of credit which have been made available to a member. Section 41(d) authorizes the President to utilize authority available to him under the Bretton Woods Agreements Act in carrying out the purposes of this section. Section 41(e) requires the Secretary of the Treasury to report on progress toward implementing the provisions of this section within six months of enactment of this section into law.

Section 42 is a sense of the Congress provision that relevant officials in the Administration should consider U.S. membership in the Bank for International Settlements and report their findings to Congress within three months after the provision becomes law.

Title I, as amended by the Banking Committee adds two new sections to the Bretton Woods Agreements Act.

Section 102 of the bill adopted by the Banking Committee adds a new section 43. (a) provides that the Secretary of the Treasury shall instruct the U.S. Executive Director of the Fund to present proposals to the Executive Board of the Fund for the purpose of ensuring that members take steps to expeditiously eliminate all import restrictions inconsistent with the GATT, or other international agreements, and which have a serious adverse impact on U.S. exports or employment. The U.S. Executive Director would consult with Congress prior to voting for any program inconsistent with these instructions.

(b) provides that as part of this effort, the U.S. Trade Representative, the Secretary of Labor, and the Secretary of Commerce shall inform the U.S. Executive Director of the Fund and the Congress of import restrictions and export subsidies maintained by other member countries which have a serious adverse impact on exports from or employment in the United States.

(c) instructs the Secretary of the Treasury to transmit an annual report to the appropriate committees of Congress on the success in reducing or eliminating the restrictions referred in subsection (a).

New Section 44 as adopted by the Banking Committee provides that the Secretary of the Treasury shall instruct the U.S. Executive Director to initiate wide consultation with other directors of the Fund with regard to developing financial and technical assistance policies which reduce obstacles to and restrictions upon international trade and investment, eliminate unfair trade and investment practices, and promote mutually advantageous economic relations.

TITLE II, SECTION 201—SHORT TITLE

Section 202 is a statement of Congressional findings recognizing the important role of lending by U.S. banks coupled with a regulatory framework encouraging prudent lending decisions.

Section 203 (1), (2) defines "appropriate federal banking agency" as the term is defined in Section 3(q) of the Federal Deposit Insurance Act (12 U.S.C. 1813(q)). With respect to bank holding companies, Edge Act and agreement corporations, the Federal Reserve Board is the "appropriate federal banking agency."

Section 203 (3), (4) defines "banking institution" as any "insured bank", as defined in Section 3(h) of the Federal Deposit Insurance Act (12 U.S.C. 1813(h)), or any subsidiary thereof, and any Edge Act or agreement corporation. The agencies may, as they deem appropriate, define the term "banking institution" to include any agency or branch of a foreign bank, or any commercial lending company owned or controlled by a foreign bank or foreign bank holding company.

Section 204 requires each bank supervisory agency to evaluate a banking institution's foreign country exposure and transfer risk and to establish examination and supervisory procedures to assure that such factors are considered in the agency's evaluation of capital adequacy.

Section 205 directs each agency to require a banking institution to establish a special reserve whenever the quality of its assets has been impaired by the protracted inability of borrowers in a country to

make payments on their external indebtedness. This section sets forth factors to be considered in making this determination. Such special reserves may not be treated as part of either capital and surplus or the institution's allowance for possible loan loss for regulator, supervisory or disclosure purposes. A banking institution may write off assets in lieu of establishing special reserves.

Section 206 directs each federal banking agency to establish the appropriate accounting treatment of fees charged by banking institutions in connection with international loans. Such procedures must require that the appropriate portion of such fees be accrued over the effective life of the loan.

Section 207 authorizes the federal banking agencies to require more frequent reporting by banking institutions of information concerning their foreign lending. It also authorizes the agencies to require public disclosure by banking institutions of information concerning material foreign country exposure.

Section 208(a) requires the Secretary of the Treasury to instruct the U.S. Executive Director of the International Monetary Fund to propose that the IMF: include in its Article IV consultations with members a closer examination of external indebtedness of borrowers in the country and make appropriate comment on such borrowings; give consideration to placing limits on public sector short- and long-term borrowing as part of any Fund-approved stabilization program; publish as part of its Annual Report an evaluation of the trend and volume of international lending as it effects the world economy and the international monetary system.

Section 208(b) requires consultation between the federal banking agencies and bank supervisors in other countries concerning supervisory policies over international lending.

Section 209 provides express authority to each federal banking agency to establish appropriate standards designed to assure that banking institutions maintain adequate levels of capital and to take such actions as may be needed for the establishment and maintenance of adequate capital, including requiring the provision of additional capital when found to be appropriate in light of the circumstances of the particular banking institution. The agencies are expected to establish reasonable time periods for a banking institution to comply with any capital requirements.

Section 210(a) authorizes the banking agencies to define terms and to issue rules, regulations or orders to carry out their authorities under this Act. This section confirms the authority of each agency to apply the Act to bank affiliates for which it is the appropriate federal banking agency.

Section 210(b) requires that the agencies adopt uniform principles and objectives to implement their respective authorities under the Act.

Section 210(c) confirms that the authorities contained in the Act are supplemental to and do not derogate from authorities otherwise provided, including the general authority of the agencies to require additional capital or reserves by a bank. In addition, this provision of the bill states that the authorities contained in Section 8 of the Federal Deposit Insurance Act may be used to ensure compliance with this Act and all rules, regulations or orders issued pursuant thereto.

Section 210(d) exempts regulations, reports and the collection of information from the Regulatory Flexibility Act (5 U.S.C. 601–610) and the Paperwork Reduction Act (44 U.S.C. 3501–3520).

Section 210(e) requires the federal banking agencies to submit annual reports to Congress for three years following enactment to advise Congress of: actions taken to implement the Act, actions that are inconsistent with uniform implementation of the Act, and further legislation that may be needed to address the concerns reflected in the Act.

CONGRESSIONAL BUDGET OFFICE—COST ESTIMATE

1. Bill number: S. 695.

2. Bill title: A bill to amend the Bretton Woods Agreement Act to authorize consent to and authorize appropriations for an increase in the United States quota in the International Monetary Fund and to authorize appropriations for increased United States participation in the General Arrangements to Borrow.

3. Bill status: As ordered reported by the Senate Committee on Banking, Housing, and Urban Affairs on April 28, 1983.

4. Bill purpose: Title I of this legislation authorizes the U.S. Governor of the International Monetary Fund (IMF) to consent to an increase in the quota of the U.S. in the Fund and authorizes the appropriation of the dollar equivalent of 5,310.8 million Special Drawing Rights (SDR) for the increase in the U.S. quota and 4,250 million SDR for an increase in loans to the IMF under the General Arrangements to Borrow (GAB). Title II establishes congressional policy concerning supervision of international lending by banking institutions.

5. Estimated cost to the Federal Government:

[By fiscal year, in millions of dollars]

	1983	1984	1985	1986	1987
Authorization level	10,464	----	----	----	----
Less: Existing appropriation	2,000	----	----	----	----
Net authorization	8,464	----	----	----	----
Estimated outlays	0	0	0	0	0

The costs of this bill fall within budget function 150.

Basic of estimate: This estimate assumes enactment of this legislation and subsequent appropriation of the dollar equivalent of the amounts authorized in a fiscal year 1983 supplemental by July 1983. The authorization is denominated in SDR's, an international reserve asset. The dollar estimate is calculated using the SDR exchange rate of February 11, 1983, ($1.0945/SDR). Two billion dollars was appripriated for the General Arrangements to Borrow in fiscal year 1962, Public Law 87–872, and remains available to offset the higher SDR authorization.

Upon entering into force, 25 percent of the increased quota subscription will be paid to the IMF in reserve assets, either SDR's or foreign currencies, the remaining 75 percent will be provided in the form of a non-interest bearing letter of credit. In exchange for the SDR's and foreign currencies, the U.S. receives an increase in its reserve position

in the IMF. This reserve position in the IMF is an interest-bearing, liquid international monetary asset that is available to the United States in case of balance-of-payment needs.

Under the letter of credit, the Treasury is committed to provide dollars upon call by the IMF. The GAB is a standby arrangement to loan additional resources to the Fund in exceptional situations to meet financing requests from member countries with balance of payments problems of a character or of aggregate size that could pose a threat to the stability of the international monetary system.

Under the guidelines established by the President's Commission on Budget Concepts and current practice, transfers of dollars to and from the U.S. Treasury and the IMF under the quota or lending arrangements are treated as exchanges of monetary assets. Cash is decreased and international monetary reserve are increased or cash is increased and international monetary reserves are decreased depending on the direction dollars flow.

Transfers between the U.S. and the IMF do affect the Treasury's cash position and borrowing requirements. The interest cost of borrowing is largely offset by remuneration (interest) on the U.S. quota and interest on loans to the IMF. Such outlays and receipts fall in budget function 900, net interest. In addition, the U.S. incurs exchange gains and losses on the U.S. reserve position in the IMF due to changes in the dollar value of the SDR.

Over the past fiscal year, the IMF has been calling on the existing U.S. letter of credit at the rate of $250 to $400 million per quarter. Because of the uncertainties regarding the future level of IMF financing; the portion of such financing that would be in dollars; and movements in market interest and exchange rates; it is impracticable to estimate the net cost of any additional U.S. transactions with the IMF associated with enactment of this legislation.

Title II of S. 695 would establish Congressional policy regarding supervision of international lending by banking institutions. It would require the Federal banking agencies, including the Board of Governors of the Federal Reserve, the Federal Deposit Insurance Corporation, and the Comptroller of the Currency to establish uniform systems regarding reserves, accounting rules for fee collections, disclosure requirements and capital adequacy.

According to the Federal banking agencies, enactment of S. 695 would not result in any significant increase in their supervisory costs. Rather than creating new regulatory authority, S. 695 would reinforce current or anticipated rules and regulations.

Section 205 of Title II would require certain banking institutions to establish a special reserve to allow for losses on international loans. Current accounting practices treat problem loans as an adjustment to capital, while S. 695 would require that the adjustment be charged against current income.

If such loans would not otherwise have been written off, this would result in a loss of tax receipts to the Federal Government. The extent of such losses is not possible to estimate with any certainty.

6. Estimated cost to State and local governments: None.

7. Estimate comparison: CBO uses the OMB estimate of interest receipts and remuneration from the IMF in budget function 900. Realized gains and losses from valuation adjustments to the U.S.

reserve position in the IMF are recognized as actuals at the end of a fiscal year, but neither OMB nor CBO attempts to estimate gains and losses in advance. Neither OMB nor CBO are estimating an outlay effect as a result of enacting this legislation and subsequent appropriation.

Both CBO and OMB are using the SDR/dollar conversion rate of February 11, 1983, in estimating the dollar equivalent of the SDR denominated authorization level.

8. Previous CBO estimate: This estimate incorporates changes made by the Senate Committee on Banking, Housing and Urban Affairs in Title II concerning supervision of international lending into the CBO cost estimate of March 18, 1983, for the bill as reported by the Senate Committee on Foreign Relations.

9. Estimate prepared by: Joseph C. Whitehill, Mary B. McGinniss.

10. Estimate approved by:

C. G. NUCKOLS
(For James L. Blum,
Assistant Director for Budget Analysis).

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